



August 29, 2006

Mr. Mark Krausse, Executive Director
Fair Political Practices Commission
428 J Street, Suite 620
Sacramento, CA 95814

Dear Mr. Krausse:

Final Report: Fair Political Practices Commission—Internal Control Review

Enclosed is the final report on the Fair Political Practices Commission's (Commission) internal control as of April 20, 2006. The Department of Finance, Office of State Audits and Evaluations (Finance), performed this review in accordance with the Financial Integrity and State Manager's Accountability Act of 1983, Government Code Section 13400 et seq.

The Commission's response is included herein. Implementation of the proposed corrective actions will help strengthen the Commission's internal control and reduce the risk of errors or irregularities.

The final report will be placed on the Finance website in accordance with Finance's policy of increased transparency. Finance appreciates the assistance and cooperation of staff and management during the review. If you have any questions, please contact Susan M. Botkin, Manager, or Dennis Mehl, Supervisor, at (916) 322-2985.

Sincerely,

Original signed by:

Diana L. Ducay, Chief
Office of State Audits and Evaluations

Enclosure

cc: Mr. Robert Tribe, Chief of Administration, Fair Political Practices Commission

AN INTERNAL CONTROL REVIEW

FAIR POLITICAL PRACTICES COMMISSION

Prepared By:
Office of State Audits and Evaluations
Department of Finance

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The Fair Political Practices Commission (Commission) has primary responsibility for the impartial administration, implementation, and enforcement of the Political Reform Act of 1974 (Act), as amended by the voters and Legislature. The objectives of the Act are to:

- Ensure that election campaign expenditure data is fully and accurately disclosed so that the voters may be fully informed and to inhibit improper financial practices.
- Regulate the activities of lobbyists and disclose their finances to prevent any improper influencing of public officials.
- Provide for the disclosure of assets and income of public officials, which may affect their official actions, to avoid any conflicts of interest.
- Ensure that the state ballot pamphlet contains useful and adequate information so that the voters will not be entirely dependent upon paid advertising for information concerning state measures.
- Eliminate laws and practices that unfairly favor incumbents to provide for fair elections.
- Provide adequate mechanisms to public officials and to private citizens to ensure vigorous enforcement of the Acts.

State managers are required to maintain internal control in the programs they administer. Internal control is defined as a process designed to provide reasonable assurance regarding the achievement of objectives in the following categories: (a) reliability of financial reporting, (b) effectiveness and efficiency of operations, and (c) compliance with applicable laws and regulations. This definition of internal control includes five interrelated components:

- *Control environment* sets the tone of an organization, influencing the control consciousness of its staff. It is the foundation for all other components of internal control, providing discipline and structure.
- *Risk Assessment* is the entity's identification and analysis of relevant risks to the achievement of its objectives, forming a basis for determining how the risks should be managed.
- *Control Activities* are the policies and procedures that help ensure management directives are carried out.
- *Information and communication* are the identification, capture, and exchange of information in a form and time frame that enable people to carry out their responsibilities.
- *Monitoring* is the process that assesses the quality of internal control performance over time.

The objective of the internal control review was to assist the Commission in complying with the Financial Integrity and State Manager's Accountability Act of 1983. Specifically, Finance assisted the Commission in determining whether: (1) assets are safeguarded from unauthorized use or disposition, (2) financial transactions are executed in accordance with management's authorizations and recorded properly to permit the preparation of reliable financial statements, and (3) financial operations are conducted in accordance with State Administrative Manual guidelines, and certain other state laws and regulations, as well as the Commission's policies and procedures.

This report is intended for the information and use of the Commission and is not intended to be and should not be used by anyone other than the specified parties. However, this report is a matter of public record and its distribution is not limited.

STAFF:

Susan M. Botkin, CGFM
Manager

Dennis Mehl
Supervisor

Georgia Folkes
Maricris Bauzon
Jake Liddicoat

EXECUTIVE SUMMARY

During the review of the Fair Political Practices Commission's (Commission) internal control conducted by the Department of Finance, Office of State Audits and Evaluations (Finance), several areas were identified where controls were in place and working as intended. Finance also identified areas where controls could be improved to reduce the risk of errors, irregularities, and material misstatements. Finance met with management and staff to discuss the following weaknesses, as well as other non-reportable findings and observations.

The Department of General Services (DGS), Contracted Fiscal Services (CFS), provides accounting services to the Commission. In addition, DGS performed a Purchasing Program Compliance Review dated March 24, 2006. Therefore, the following comments are limited to functions or activities performed by the Commission and not performed by CFS nor addressed by the DGS review.

Administrative controls: The Commission does not have adequate written procedures for a number of business functions.

Cash Receipts: Controls are in place to ensure the collection and reporting of cash receipts. However, checks are not always endorsed and deposited in a timely manner.

Personnel/Payroll: Controls over personnel/payroll functions ensure timely monthly payroll processing, appropriate separation of duties, correct authorizations, and properly maintained leave records. However, clearance procedures for separating employees need to be improved.

Purchasing: Controls are in place to ensure that purchase documents and contracts are recorded timely and accurately, and approved by responsible staff. However, there is inadequate segregation of duties.

Fixed Assets: Controls over fixed asset functions provide adequate separation of duties, updated authorizations and required inventory counts. However, the inventory cannot be performed accurately, because property acquisitions, transfers, and dispositions have not been consistently recorded.

Information Security: Comprehensive operational recovery and risk management plans have been developed to insure business continuity in the event of a disaster, and controls are in place to control access to sensitive data. However, data has not been formally classified in writing and there is no duty statement for the Information Security Officer.

There were no significant findings for the Commission's budget, disbursements, revolving fund, financial reporting, and contract functions.

For further analysis of the findings summarized above, see the *Findings and Recommendations* section of this report.

This report is intended to assist the Commission's management in focusing attention on areas of risk and in strengthening internal control and improving operations.



AUDITOR'S REPORT

Mr. Mark Krausse, Executive Director
Fair Political Practices Commission
428 J Street, Suite 620
Sacramento, CA 95814

The Department of Finance, Office of State Audits and Evaluations (Finance), has reviewed the Fair Political Practices Commission's (Commission) internal control as of April 20, 2006 for conformity with Government Code Section 13400 et seq. Finance's review included obtaining an understanding of internal control through observations and interviews, identifying risks, testing and evaluating the design and operating effectiveness of the internal control, and performing other procedures Finance deemed necessary under the circumstances.

The Commission's management is responsible for establishing and maintaining adequate internal control. This responsibility, in accordance with Government Code Section 13400 et seq., includes documenting internal control, communicating control requirements to employees, and assuring that the internal control is functioning as prescribed. In fulfilling its responsibility, management is required to assess the expected benefits and costs of its control procedures.

The objectives of internal control are to provide reasonable, but not absolute, assurance that:

- Assets are safeguarded against loss from unauthorized use or disposition.
- Transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of reliable financial statements.
- Financial operations are conducted in accordance with policies and procedures established in the State Administrative Manual, and certain other state laws and regulations, as well as the Commission's policies and procedures.

Because of inherent limitations in any internal control, misstatements due to error or fraud may occur and not be detected. Also, projections of any review of internal control in future periods are subject to the risk that the internal control may become inadequate because of changing conditions, or that compliance with control policies or procedures may decline.

Finance noted certain matters involving the Commission's internal control as of April 20, 2006, and its operation that are considered to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control that, in our judgment, could adversely affect the Commission's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

A material weakness is a condition that precludes the Commission's internal control from providing reasonable assurance that material misstatements in the financial statements will be prevented, or detected on a timely basis. Finance believes the reportable conditions concerning Administrative Controls and Cash Receipts are material weaknesses. These weaknesses and other reportable conditions are described in the *Findings and Recommendations* section of this report.

This report is intended for the information and use of the Commission's management, and is not intended to be used by anyone other than the designated parties. However, this report is a matter of public record and its distribution is not limited.

Original signed by:

Diana L. Ducay, Chief
Office of State Audits and Evaluations
(916) 322-2985

April 20, 2006

FINDINGS AND RECOMMENDATIONS

The Department of Finance, Office of State Audits and Evaluations (Finance), reviewed the accounting and administrative controls within the Fair Political Practices Commission (Commission). During Finance's review, it was noted that a number of controls were functioning as intended. However, Finance also identified areas where controls are not in place and where corrective action is necessary, as described below.

Administrative Controls

Administrative or managerial controls relate to operational efficiency, adherence to managerial policies, and management's authorization of transactions. Department management is responsible for overseeing activities conducted within their agencies. This responsibility includes the establishment and maintenance of internal accounting and administrative controls over operations.

FINDING 1 Inadequate Documentation of Policies and Procedures

Condition: There is a lack of written policies and procedures for the following functions:

- Cash Receipts
- Account Receivables, Enforcement Division
- Cash Disbursements
- Contracts
- Fixed Assets
- Information Technology
- Personnel and Payroll

Criteria: State Administrative Manual (SAM) Section 20050 states that the elements of a satisfactory system of internal accounting and administrative controls shall include a system of authorization and record keeping procedures adequate to provide effective accounting controls.

Recommendation: Ensure all operational processes and procedures are appropriately documented and updated.

Cash Receipts

Effective controls over cash receipts are necessary to ensure all amounts are properly safeguarded, and deposited in a timely manner. The following weakness relative to Cash Receipts was observed.

FINDING 2 Inadequate Check Endorsements, Forwarding, and Safeguarding

Condition: Checks are not restrictively endorsed on a timely basis. Checks accumulate up to one week before they are endorsed for deposit. Furthermore, they are not forwarded to Contracted Fiscal Services (CFS) on a timely basis. Ten of twenty-seven checks reviewed were forwarded to CFS 15 to 48 days after the check receipt date. This results in potential loss or misplacement, and lost interest because of untimely deposits.

Criteria: SAM Section 8023 states that all checks, money orders, and warrants received for deposit will be restrictively endorsed for deposit as soon as possible after receipt, but no later than the end of the working day.

SAM Section 8032.1 states that accumulated receipts of any amount will not remain undeposited for more than ten working days.

Recommendation: Establish procedures to restrictively endorse checks on the day of receipt, and ensure checks are forwarded to CFS in a timely manner.

Personnel/Payroll

Effective internal controls over personnel/payroll are necessary to ensure that adequate clearance procedures exist for separating employees. The following weaknesses were identified.

FINDING 3 Inadequate Review of Employee Separations

Condition: The final payroll warrant calculation of a separating employee is not reviewed by a supervisor or other independent party. Establishment of this procedure could prevent potential errors in payroll calculations.

There is no single point of accountability for separating employees to clear outstanding advances, turn in state owned property, and clear information system access. This could result in undetected losses of state assets.

Criteria: SAM Section 8580.4 states that final warrants are not to be distributed to separating employees until the agency is assured that all outstanding travel and salary advances and other obligations have been cleared.

Recommendations: Ensure that all separation payroll warrant calculations are adequately reviewed prior to release of warrant.

Ensure that any outstanding advances, state owned property, and information system accesses are cleared prior to separation.

Purchasing

Effective internal controls over purchasing are necessary to ensure that goods and services ordered are received. The following weakness was identified.

FINDING 4 Inadequate Segregation of Duties Over Purchasing

Condition: Segregation of duties over the purchasing function is weak. The employee who orders merchandise and equipment also performs the receiving function.

Criteria: Government Code Section 13403 states that a satisfactory system of internal accounting and administrative controls shall include a plan of organization that provides segregation of duties appropriate for proper safeguarding of state assets.

Recommendation: Ensure there is adequate segregation of incompatible duties.

Fixed Assets

Adequate control of property transactions must be in place to protect against and detect the unauthorized use or loss of state property. The following weakness was identified.

FINDING 5 Inventory Records Are Inaccurate

Condition: Inventory records are inaccurate. Only 48 percent of the 61 items tested were correctly listed on the inventory records. This is primarily caused by not recording acquisitions, transfers and dispositions of property.

Criteria SAM Section 8600 provides standard procedures for recording the acquisition, transfer, and dispositions of property.

Recommendation: Ensure compliance with required property accounting procedures.

Information Security

Effective information security controls are necessary to ensure compliance with the state's security and data integrity policies. The following weaknesses were observed relative to information security.

FINDING 6 Data Has Not Been Formally Classified in Writing

Condition: The Commission's data has not been formally classified in writing. Agencies are required to classify data elements as public, confidential, or sensitive.

Criteria: SAM Section 4841.2 states, in part, that each agency must provide for the integrity and security of its automated files and databases by ensuring that each automated file or database is identified as to its information class (SAM Section 4831.3) in accordance with law and administrative policy.

Recommendation: Classify the Commission's data to protect against unintentional or unauthorized access and disclosure.

FINDING 7**Lack of Job Description for Information Security Officer**

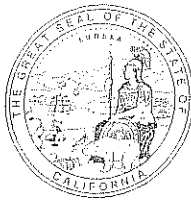
- Condition: The Commission does not have a specific charter/job duties for the functions and duties of the Information Security Officer (ISO). The job expectations, duties, authority, and who the ISO reports to are not clearly defined in writing.
- Criteria: SAM Section 4842.2 indicates that an agency's information security and risk management practices include written documentation of specific responsibilities.
- Recommendation: Develop and approve a written charter/job duty statement for the ISO.

CONCLUSION

The Department of Finance, Office of State Audits and Evaluations' (Finance), review of the Fair Political Practices Commission's (Commission) internal control presents opportunities for management to correct identified weaknesses and improve its operations. Finance believes internal control would be strengthened and the Commission would operate more effectively if the Commission implements the recommendations. The reportable conditions, if left uncorrected, increase the risk that material errors or irregularities could occur and remain undetected, and the material weaknesses, if left uncorrected, could adversely affect the Commission's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

The findings in this report are based on fieldwork performed between March 13, 2006 and April 20, 2006. Finance presented these findings to the Commission on May 11, 2006 and at the exit conference held on May 16, 2006.

AGENCY RESPONSE



FAIR POLITICAL PRACTICES COMMISSION

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August 17, 2006

Ms. Diana L. Ducay, Chief
Department of Finance
Office of State Audits and Evaluations
300 Capitol Mall, Suite 801
Sacramento, CA 95814

Dear Ms. Ducay:

We are providing this letter in response to the draft report on the Fair Political Practices Commission internal control provided to us by your office. We appreciate the time and effort your staff took in reviewing our operations and the suggestions provided. Attached are comments regarding the recommendations contained in the report.

Should you have any questions, please feel free to contact either myself or our Budget Officer, Tina Z. Bass at (916) 322-5660.

Sincerely,

Original signed by:

Robert Tribe, Chief of Administration
Fair Political Practices Commission

Attachment

Cc: Ms. Susan M. Botkin, Manager, DOF
Mr. Dennis Mehl, Supervisor, DOF

Fair Political Practices Commission

Response to Department of Finance Internal Control Review April 2006

The Department of Finance, Office of State Audits and Evaluations conducted a review of the accounting and administrative controls of the Fair Political Practices Commission in April 2006. The review noted that many of the Commission's controls "were functioning as intended." However, there were seven findings noted in the report. Each finding is summarized below along with Commission staff's proposed action.

- **Finding 1 Inadequate Documentation of Policies and Procedures**

Written policies and procedures for some of the Commission's functions were determined to be outdated, inadequate or unavailable. Commission staff agree with the importance of written policies and are working to appropriately document and update operational processes and procedures.

- **Finding 2 Inadequate Check Endorsements, Forwarding, and Safeguarding**

Checks are required per SAM Section 8023 to be endorsed by the end of the working day and deposited within 10 working days. The report found that these requirements were not being met consistently.

Enforcement staff have been reviewing the validity of payments prior to their endorsement and deposit which includes handling by support staff and review by the attorney or consultant handling the case. This review has delayed the endorsement and deposit of checks particularly when the attorney or consultant is unavailable. New procedures have been developed to expedite this process and ensure that endorsement and deposit are timely. These procedures will be implemented after presentation to staff at this month's Enforcement Division staff meeting.

- **Finding 3 Inadequate Review of Employee Separations**

The report recommends that separation payroll warrant calculations be reviewed prior to release of the warrant and that all outstanding advances, state owned property and information system accesses are cleared prior to separation.

Currently, the Commission has a procedure for handling employee separations. Staff plan to integrate any element that has been overlooked into the current procedures creating a comprehensive employee separation checklist which will be provided to each division.

- **Finding 4 Inadequate Segregation of Duties Over Purchasing**

The segregation of duties was found inadequate as the same employee who purchases often performs the receiving function.

The Commission has experienced staff reductions over the past few years due to budgetary constraints. One area impacted was the administrative area. Previously, additional staff were available in the reception area and purchasing and receiving functions could be conducted by different employees. Currently, one staff person performs the purchasing function. This employee also staffs the reception function and therefore when no one else is available performs the receiving function. We are currently looking at bringing a staff person from the Technical Assistance Division in to perform the reception function. This would allow adequate segregation of duties and resolve the finding.

- **Finding 5 Inventory Records Are Inaccurate**

The review found that inventory records are inaccurate. The raising of this issue by the review has alerted relevant staff who are working on correcting the deficit. However, due to lack of experience in this area, additional staff training may be required to fully resolve this finding.

- **Finding 6 Data Has Not Been Formally Classified in Writing**

The data was found in need of classification as to whether it is public, confidential or sensitive. The information technology staff are now aware of this issue and agree with the finding.

- **Finding 7 Lack of Job Description for Information Security Officer**

The review identified the need for a specific written job description enumerated for the Commission's Information Security Officer. Management agree with the value of this finding and will implement.